Save the Cooperative Way of Business

by

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The following statement was published on page 23 of Buckeye Farm News, January 1980, under the heading of Farm Bureau's Policies for 1980:

> "The Capper Volstead Act has served the farmers and consumers of this nation by permitting farmers to help solve their business problems cooperatively. We oppose any efforts to weaken or repeal this act.
>
> We believe that the U.S.D.A. should continue as the agency responsible to monitor the activities of cooperatives and their adherence to the Capper Volstead Act.
>
> Because of changing economic conditions we feel the 8 percent dividend limit on cooperative stock is unreasonable. We feel this limit should be permitted to fluctuate with the economy, possibly using the prime rate as a guide......"

This appears to be a conflicting policy where it first asks not to weaken the Capper Volstead Act and later proposes a change in the second requirement of the Capper Volstead Act, as well as Section 1729 of the Ohio Revised Code.

The Ohio Cooperative Marketing Act is Section 1729. Two excerpts are:

> "Associations shall be deemed nonprofit inasmuch as they are not organized to make profit for themselves as such, or for their members as such, but only for their members as producers."

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> "The association shall limit its dividends on stock to any amount not greater than eight (8) percent per annum; and all its other net income, less specified reserves which shall be provided for in the

bylaws, shall be distributed to its members only on the basis of patronage. Any receipts or dividends from subsidiary corporations, or from stock or other securities owned by the association, shall be distributed accordingly."

Cooperatives are one of 4 ways of doing business in the United States. They are: (1) Sole Proprietor, (2) Partnership, (3) Investor Corporation, and (4) Cooperative Corporation.

The basic cooperative principles that differentiate cooperative corporations from investor corporations are:

- Operations at Cost (The firm does not keep the profits or margins made from all business transactions but returns these margins or profits to those who use the business.)
- Democratic Control (People, not dollars, vote. Voting in a cooperative is not determined by one's investment.)
- Limited return on equity capital. (Profits or margins can not be paid out on the basis of investment and to discourage paying out margins to investors as well as discourage outside speculative investment and encourage member financing, a limit of 8 percent was placed on stock dividends by IRS for 521 cooperatives, Capper Volstead Act and state laws.)
- Financed by members (To insure member control and larger patronage refunds to members.)
- Education of members about cooperatives as a unique way of doing business.

Those Ohio agribusiness firms whose owners desire to distribute their margins or profits to investors should re-charter their firm under Section 1701 rather than destroy the cooperative legislation.

Section 1729 should remain unchanged for those persons who desire to organize a cooperative.

The Capper Volstead Act permits farmers to join together in associations, provided the association is:

Operated for the mutual benefit of the "members" and conforms to one or both of the following requirements:

First - that no member of the association is allowed more than one vote because of the amount of stock or membership capital he may own therein, or,

Second - that the association does not pay dividends on stock or membership capital in excess of 8 per centum per annum.

Please observe that only one of the two above requirements must be met! Some Ohio agribusinesses have already elected not to conform to the first.

The National Council of Farmer Cooperatives is on record as favoring no change in the Capper Volstead Act.

It is a fact that the Capper Volstead Act and Section 1729 were both enacted nearly 60 years ago. It is also a fact that at that time (1920s) cooperatives were not required to include the dividends they paid on stock in their taxable income. In 1980 those "farmers, fruit growers or like associations organized and operated on a cooperative basis---marketing or purchasing association--ULTIMATELY TURNING BACK ALL NET PROCEEDS to member and non-member patrons on the basis of quantity or value of business conducted by each with the association, and limiting return on equity to 8 percent, and limited accumulation of reserves, and if they do more business with members than with non-members and do no more than 15% of the total business with non-members, non-producers," may have 521 classification by IRS, and can exclude the dividends they pay on stock from their taxable income. Therefore, those firms that have elected not to meet the 521 requirements of IRS must pay IRS taxes on the dividends they pay on equity capital. For example, a firm with a 46% IRS tax rate that pays $10,000 dividends on equity capital would also pay IRS $8,519 or to put it another way, to pay $10,000 stock dividend would require $18,519, with $8,519 going to IRS and $10,000 to the investor as a stock dividend. This same $18,519 could, in a cooperative, be paid out as patronage refund or used to retire old non-cash patronage (equity) with the total $18,519 going into the income of farmer members.

If the dividend rate of cooperative stock were permitted to fluctuate with the prime interest rate, would this attract more equity capital from farmer members? Many observers report that this has not been the case in those states which have changed their law.

If the rate of interest paid to those who purchase equity capital, as an investment, is permitted to fluctuate with the prime interest rate, would it not also be fair for these same firms to pay the prime interest rate on the non-cash portion of the patronage refund allocated to users? It would appear to be a "ripoff" if investors were paid 15% interest and users were paid nothing for their equity (non-cash patronage) held in the firm by the board of directors.

Cooperatives are one of the four ways of doing business in the United States. Those firms that do not want to operate as a cooperative form of business and return their profits to users should re-charter as investor corporations under Section 1701 of the Ohio Revised Code.

Section 1729 of the Ohio Revised Code and the Capper Volstead Act should be left as is for those who choose to organize and operate under the cooperative way of business.